by the same amount. In other words, consumer prices rose in relation to wholesale and commodity prices.

The relationship still holds even today during a recession, except that now in absolute terms, consumer prices are rising instead of falling. This is because the magnitude of monetary inflation is much greater than in past cycles. So, relative to capital goods, all recessions are "inflationary recessions." It's just that such a relationship didn't become obvious until the Consumer Price Index continued to rise in the 1973-1975 recession and the 1980-1981 recession.

If you want to learn more about this aspect of Austrian economics, I recommend the following books, all available from the Institute: *What Has Government Done to Our Money?*, by Murray N. Rothbard ($5), *America's Great Depression* also by Rothbard ($20), *An Introduction to Austrian Economics* by Thomas C. Taylor ($6), and *The Austrian Theory of the Trade Cycle* by Ludwig von Mises and others ($5); shipping charge: $2.75 with each order.

All show that the only way that we can escape from the business cycle is through the establishment of sound money (i.e., a gold standard and no central bank) and the free market. If we are ever able to do so, the Austrian school of economics will deserve the credit.

Money Inflation and Price Inflation

Murray N. Rothbard

In the last few months, the Reagan administration seems to have achieved the culmination of its "economic miracle" of the last several years: while the money supply has skyrocketed upward in double digits, the consumer price index has

remained virtually flat. Money cheap and abundant, stock and bond markets booming, and yet prices remaining stable: what could be better than that? Has the president, by inducing Americans to feel good and stand tall, really managed to repeal economic law? Has soft soap been able to erase the need for "root-canal" economics?

In the first place, we have heard that song before. During every boom period, statesmen, economists, and financial writers manage to find reasons for proclaiming that now, *this time*, we are living in a new age where old-fashioned economic law has been nullified and cast into the dust bin of history. The 1920s is a particularly instructive decade, because then we had expanding money and credit, and a stock and bond market boom, while prices remained constant. As a result, all the experts as well as the politicians announced that we were living in a brand "new era," in which new tools available to government had eliminated inflations and depressions.

What were these marvelous new tools? As Bernard M. Baruch explained in an optimistic interview in the spring of 1929, they were (a) expanded cooperation between government and business; and (b) the Federal Reserve Act, "which gave us coordinated control of our financial resources and . . . a unified banking system." And, as a result, the country was brimming with "self-confidence." But, also as a result of these tools, there came 1929 and the Great Depression. Unfortunately both of these mechanisms are with us today in aggravated form. And great self confidence, which persisted in the market and among the public into 1931, didn't help one whit when the fundamental realities took over.

But the problem is not simply history. There are very goods reasons why monetary inflation cannot bring endless prosperity. In the first place, *even if there were no price inflation*, monetary inflation is a bad proposition. For monetary inflation is counterfeiting, plain and simple. As in counterfeiting, the creation of new money simply diverts resources

from producers, who have gotten their money honestly, to the early recipients of the new money—to the counterfeiters, and to those on whom they spend their money.

Counterfeiting is a method of taxation and redistribution—*from producers to counterfeiters* and to those early in the chain when counterfeiters spend their money and the money gets respent. Even if prices do not increase, this does not alleviate the coercive shift in income and wealth that takes place. As a matter of fact, some economists have interpreted price inflation as a desperate method by which the public, suffering from monetary inflation, tries to recoup its command of economic resources by raising prices at least as fast, if not faster, than the government prints new money.

Secondly, if new money is created via bank loans to business, as much of it is, the money inevitably distorts the pattern of productive investments. The fundamental insight of the "Austrian," or Misesian, theory of the business cycle is that monetary inflation via loans to business causes overinvestment in capital goods, especially in such areas as construction, long-term investments, machine tools, and industrial commodities. On the other hand, there is a relative underinvestment in consumer goods industries. And since stock prices and real estate prices are titles to capital goods, there tends as well to be an excessive boom. It is not necessary for consumer prices to go up, and therefore to register as price inflation. And this is precisely what happened in the 1920s, fooling economists and financiers unfamiliar with Austrian analysis, and lulling them into the belief that no great crash or recession would be possible. The rest is history. So, the fact that prices have remained stable recently does not mean that we will not reap the whirlwind of recession and crash.

But why didn't prices rise in the 1920s? Because the enormous increase in productivity and the supply of goods offset the increase of money. This offset did not, however, prevent a

crash from developing, even though it did avert price inflation. Our good fortune, unfortunately, is not due to increased productivity. Productivity growth has been minimal since the 1970s, and real income and the standard of living have barely increased since that time.

The offsets to price inflation in the 1980s have been very different. At first, during the Reagan administration, a severe depression developed in 1981 and continued into 1983, of course dragging down the price inflation rate. Recovery was slow at first, and in the last few years, three special factors have held down price inflation. An enormous balance of trade deficit of $150 billion was eagerly enhanced by foreign investors in American dollars, which kept the dollar unprecedentedly high, and therefore import prices low, despite the huge deficit.

Secondly, and unusually, a flood of cash dollars stayed overseas, in hyperinflating countries of Asia and Latin America, to serve as underground money in place of the increasingly worthless domestic currency. And thirdly, the well-known collapse of the OPEC cartel at last brought down oil and petroleum product prices to free-market levels. But all of these offsets are obviously one-shot, and are rapidly coming to an end. In fact, the dollar has already declined in value, compared to foreign currencies, by about 30% since last September.

We are left with the fourth offset to price inflation, the increased willingness by the public to hold money rather than spend it, as the public has become convinced that the Reagan administration has discovered the secrets to an economic miracle in which prices will never rise again. But the public has not been *deeply* convinced of this, because real interest rates (interest rates in money minus the inflation rate) are at the highest level in its history. And interest rates are strongly affected by people's expectations of future price inflation; the higher the expectation, the higher the interest rate.

We may therefore expect a resumption of price inflation before long, and, as the public begins to wake up to the humbug nature of the "economic miracle," we may expect that inflation to accelerate.

First Step Back to Gold

Murray N. Rothbard

September 1986 is an historic month in the history of United States monetary policy. For it is the first month in over fifty years—thanks to the heroic leadership of Ron Paul during his four terms in Congress—that the United States Treasury has minted a genuine gold coin.

Gold coins were the standard money in the United States until Franklin Roosevelt repudiated the gold standard and confiscated the gold coins Americans possessed in 1933. Not only were these gold coins confiscated, under cover of the depression emergency, but possession not only of gold coins but of all gold (with the exception of designated amounts grudgingly allowed to collectors, dentists, jewelers, and industrial users) was prohibited.

During the 1970s, Congress made possession of gold by Americans legal, and now the Treasury itself acknowledges at least some monetary use by minting its own gold coins. We have come a long way, in only a decade, from total outlawry to Treasury minting.

It is true that the political motives for the new coin were not all of the purest. Some of it was a way of trying to attract the gold coin business from the South African krugerrands, which somehow have acquired a taint of apartheid by their mere production in South Africa. But the important thing is